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August 10, 1995

TO: Technical Accounting Review Committee

FROM: Jeff Rowitz, Chairman

RE: Next Meeting

The next meeting of the Technical Committee will be held on Wednesday, September 6, 1995 at 10:00 a.m. at the Willowbrook Village Hall. Our topic for discussion will be the Preliminary Views (PV) document on the financial reporting model project.

I have included a copy of the Committee's previous position on the reporting model project in order to refresh everyone's memory. We will need to evaluate our previous position against the PV, and determine if we want to make any changes.

If you are unable to attend the meeting, please let me know by September 5. Also, if you cannot attend, if you would fax your comments to me by September 5, I will include them in our discussions.

ILLINOIS
GOVERNMENT FINANCE
OFFICERS ASSOCIATION
Incorporated 1958

October 13, 1994

Mr. David R. Bean
Director of Research
Project No. 3-4
Governmental Accounting Standards Board
401 Merrit 7, P.O. Box 5116
Norwalk, Connecticut 06856-5116

Dear Mr. Bean,

The Illinois Government Finance Officers Association is an organization in excess of 600 members comprised of public finance officers, auditors, accountants, bankers and others interested in public finance in the state of Illinois. Our organization is dedicated to the common goal of developing better understanding and cooperation among those concerned with public jurisdictions and other objectives of mutual interest to public finance officers.

To accomplish this goal, the IGFOA has several committees actively involved in the achievement of greater success in efficiency and service of government. The Technical Accounting Review Committee (TARC) was created for the purpose of reviewing accounting, auditing and financial reporting requirements as they effect the membership of IGFOA. In fulfilling these objectives, we have consistently responded to due process documents issued by the Governmental Accounting Standards Board (GASB) and are submitting our response to the Invitation to Comment (ITC), <u>Governmental Financial Reporting Model</u> (Project No. 3-4). In addition, this response will serve as our written testimony for the public hearing to be held on October 14, 1994, in Chicago, Illinois.

The committee has reviewed Model 1 and Model 2 in the ITC and can not support the basic concepts of either model in their entirety. Therefore, we have developed an alternative model that incorporates certain elements of both models contained in the ITC and certain elements of the current model endorsed in GASB Statement No. 1, <u>Authoritative Status of NCGA Pronouncements and AICPA Industry Audit Guide</u>. The following is a discussion of the alternative model that we are recommending, in a topical format.

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AGGREGATED REPORTING

We support the basic concept in the ITC of aggregated reporting beyond the traditional aggregation by fund type currently presented in the general purpose financial statements and the development of a new top level in the financial reporting pyramid. However, we do not believe that aggregation at this level into either a single column or a total column is appropriate due to the different types of services that are provided by state and local governments and the need to use different measurement focuses to report on the financial results of providing those services.

Therefore, we recommend that the top of the pyramid contain three columns, one for tax financed services of the primary government, one for fee financed services of the primary government and one for discretely presented component units as defined in GASB Statement No. 14, The Financial Reporting Entity. A total column or columns should not be required or allowed to be presented since the use of different measurement focuses would not be conducive to a consolidation nor provide any meaningful data for a financial statement user. In addition, we do not believe that comparative information should be permitted at this level for the same reasons.

This type of presentation would provide a user with an overview of the financial position and results of operations of the reporting entity in a clear and concise manner and provide accountability for how certain government services are financed. Moreover, we would measure interperiod equity at this level to enable a user to determine whether or not current year resources were sufficient to cover the total cost of providing those services.

MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

We believe that there are inherent differences between tax financed and fee financed services. Therefore, these services should be measured using different measurement focuses. For tax financed services, we believe that the total financial resources measurement focus adopted in GASB Statement No.11 should be used. For fee financed services, we recommend the continued use of the total economic resources measurement focus. Our rationale for this position is that general fixed assets related to tax supported services do not produce revenue and should not be reported, while fixed assets related to fee financed services are used towards the generation of fees.

In addition, we adamantly disagree with the use of different measurement focuses or bases of accounting for the same type of services reported at different levels of the financial reporting pyramid. In our opinion, this would be extremely confusing for the financial statement user. Therefore, we recommend the use of the same measurement focuses and bases of accounting for the same services throughout the entire financial reporting pyramid.

METHOD OF AGGREGATION

We commend the GASB at attempting to simplify governmental financial reporting by eliminating certain fund types and account groups. We strongly endorse the concept of eliminating both the general long-term debt account group and the general fixed asset account group. The general long-term debt account group has long been misunderstood by financial statement users and abused by financial statement preparers. Likewise, the general fixed asset account group has always been misleading due to reporting fixed assets at historical cost while providing no useful financial information. As previously noted, fixed assets acquired or used in tax financed services do not directly produce a revenue source and therefore, should not be reported at any level of the financial reporting pyramid in tax financed funds.

We recommend that debt issued for the purchase of capital assets be recorded as a liability in the fund where the revenue stream is derived to repay the debt. The offset to this liability would be displayed in the Net Resources section as net noncurrent financial resources provided (required) for net long-term liabilities. This would allow the reporting of the purchase of capital assets as well as the repayment of debt principle and interest to be reported as expenditures, which is consistent with budgetary practices in the state and local government industry.

We also commend GASB for recommending the elimination of trust and agency funds from the financial reporting model. This fund classification has also long been misunderstood by financial statement users and abused by financial statement preparers. We agree with the concept in the ITC that financial resources currently reported in trust and agency funds that are available to finance either tax financed services or fee financed services be reported in those funds. If the resources are not available to finance operations of the entity then the resources should not be reported either on the face of the financial statements at any level or displayed in the notes to the financial statements. The only disclosures necessary would be the current funding/liability disclosures that were recommended by GASB in the exposure draft (ED), Employers Accounting for Pension Costs and the reference to separately issued financial statements for these activities.

In addition, we recommend that all transactions between funds within the same fund classification be eliminated for financial reporting purposes at this level. Transactions between tax financed and fee financed classifications as well as discretely presented component units should be presented but identified separately on the face of the financial statements to emphasize the inter-entity relationship of the transaction.

BUDGETARY REPORTING

We strongly support budget to actual comparisons in the financial statements to demonstrate legal compliance. However, these comparisons should be made using the final amended budget only, since this is the legal authority to spend public resources. The actual figures to compare to the budget should be on the same measurement focus and basis of accounting as the budget.

If the true intent of budgetary reporting in external financial reports is to demonstrate legal compliance, then budgetary reporting should only be presented at the fund classification level that the budget is adopted. For example, if a budget is adopted by individual funds, then the only reporting of budget versus actual should be at the individual fund level at the legal level of control. Aggregating this information to some higher level (e.g., tax financed classifications or fee financed classifications) is absolutely meaningless and provides no useful information since this does not even attempt to demonstrate legal compliance. Likewise, if the budget is adopted at an aggregated level, then it should be presented only at the aggregated level. If the display of budget versus actual information is intended for purposes other than demonstrating legal compliance, then it should be eliminated from GAAP based external financial reports.

This is the only financial statement/schedule that should incorporate any form of budgetary terminology or display. We strongly disagree with the proposed reporting of a "budgetary fund balance" on a gaap based financial statement. The figure displayed in the ITC is little more than a plug figure that would do nothing but confuse a financial statement user.

STATEMENT OF CASH FLOWS

We disagree with the recommendation in the ITC that requires the presentation of a cash flow statement for governmental funds (tax financed classification). If the total financial resources measurement focus is used and if budgetary reporting is required using the budgetary basis for tax financed classifications, then sufficient information on the inflows and outflows of financial resources will be presented on these financial statements and a statement of cash flows would provide no additional meaningful information. Instead, this would place an additional burden on report preparers and attestors without providing a benefit for financial statement users.

COMBINED FINANCIAL STATEMENTS

The need for the development of a new top of the pyramid level of financial reporting to provide users with a comprehensive overview of the tax financed classification, fee financed classification and discretely presented component units supports the historical viewpoint discussed in the ITC that the combined financial statements have not nor ever will satisfy the information needs of financial statement users. Therefore, we recommend that the traditional combined financial statements be eliminated.

GENERAL PURPOSE FINANCIAL STATEMENTS (GPFS)

We believe that the concept of "liftable" GPFS is inherently flawed and detracts from the CAFR. Consequently, we do not believe that any portion of the CAFR should be designated as the GPFS. If less detailed information is needed for certain situations, this data could be extracted from the CAFR and presented as "condensed financial statements" not in conformity with GAAP. Consistent with this view, we believe that the notes to the financial statements should be placed before the combining and individual fund statements. The notes then would explain all financial statements in the report and would eliminate the need for individual fund disclosures.

COMBINING AND INDIVIDUAL FUND STATEMENTS

The combining statements would be presented by major fund for each of the three classifications reported at the TOP. Fund type data would no longer be presented consistent with the elimination of the combined financial statements. These statements would require a total column that would tie forward to the TOP of the reporting pyramid. Minor funds could be aggregated into a single column at this level. Individual fund statements would only be required if necessary to demonstrate legal compliance (e.g., budget versus actual). Additionally, individual fund financial statements could be presented at the discretion of the report preparer.

NOTES TO THE FINANCIAL STATEMENTS

As part of the reporting model project, the GASB should review the current required notes to the financial statements and eliminate any unnecessary or redundant disclosures. Many of the current disclosures tend to attempt to teach governmental accounting to the financial statement users rather than to inform them. Moreover, the requirement to present summary or other financial information in the notes that is presented elsewhere in the report should be eliminated consistent with the elimination of "liftable" general purpose financial statements previously recommended.

STATEMENT FORMAT

BALANCE SHEET - We believe that a traditional balance sheet can and should be presented at all levels of the reporting pyramid. Furthermore, we recommend that a classified balance sheet format be utilized to segregate current and noncurrent financial resources and current and noncurrent liabilities. Equity classifications would be segregated between current (current financial resources minus current liabilities) and noncurrent (noncurrent financial resources minus noncurrent liabilities).

OPERATING STATEMENT - The operating statement would utilize the same format regardless of the measurement focus used to allow the presentation of one operating statement at the TOP. This statement should allow flexibility in formatting so as not to be burdensome or limiting to report preparers and users. However, we would recommend that the expenditures/expenses related to capital assets (e.g. debt service and capital outlay expenditures for tax financed classifications and depreciation expense for fee financed classifications) be formatted in a separate category. In addition, proceeds of debt for fee financed classifications and transactions between classifications should also be reported in a separate category. This would provide the user with a measure of interperiod equity at <u>all</u> levels of the reporting pyramid.

We sincerely appreciate the opportunity to respond to this ITC and to testify at this public hearing. If the board has any questions or needs any further clarification on any issue, please let me know.

Sincerely,

Jeffrey L. Rowitz
Chairman
Technical Accounting Review Committee